

## Message Text

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ACTION EUR-12

INFO OCT-01 EA-12 IO-14 ISO-00 AID-05 CIAE-00 EB-08  
FRB-01 INR-10 NSAE-00 ICA-20 XMB-04 OPIC-06 SP-02  
LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-07 CEA-01  
L-03 H-02 PA-02 DOE-15 SOE-02 DOEE-00 /153 W  
-----056767 022007Z /45

P R 021806Z AUG 78  
FM AMEMBASSY LONDON  
TO SECSTATE WASHDC PRIORITY 8753  
TREASURY DEPT WASHDC PRIORITY  
INFO AMEMBASSY BONN  
AMEMBASSY BRUSSELS  
AMEMBASSY DUBLIN  
AMEMBASSY PARIS  
AMEMBASSY ROME  
AMEMBASSY TOKYO  
AMCONSUL BELFAST  
AMCONSUL EDINBURGH  
USMISSION GENEVA  
USDOC WASHDC

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USEEC ALSO FOR EMBASSY  
USOECN ALSO FOR EMBASSY  
USMTN

DEPARTMENT PASS FEDERAL RESERVE BOARD; TREASURY FOR  
DONL/D / SYIRUD, OASIA

E.O. 11652: N/A  
TAGS: ECON, UK  
SUBJECT: ECONOMIC DEVELOPMENTS FOR PERIOD JULY 27 - AUG 2

SUMMARY: THE CONFEDERATION OF BRITISH INDUSTRY'S LATEST  
SURVEY INDICATES THAT BUSINESS OPTIMISM HAS NOT INCREASED  
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IN LINE WITH INDICATIONS OF NATIONAL OUTPUT. THE BANK OF  
ENGLAND RELEASES RESERVES TO THE BANKING SYSTEM HELPING  
TO EASE PRESSURES IN THE MONEY MARKET. STERLING'S POSI-  
TION ON THE SIDELINES IS UNDERLINED BY A MODEST, \$193  
MILLION, RISE IN JULY RESERVES. END SUMMARY

1. CBI QUARTERLY TRENDS SURVEY.

THE CBI'S LATEST QUARTERLY TRENDS SURVEY DOES NOT APPEAR TO REFLECT THE RISE IN RETAIL SALES VOLUME INDICATED BY THE OFFICIAL STATISTICS. IT MUST BE KEPT IN MIND, HOWEVER, THAT THE RESPONSES TO THE SURVEY ARE CONSISTENT WITH MANY LEVELS AND DIRECTIONS OF INDUSTRIAL AND FINANCIAL ACTIVITY. THERE WERE 2,014 RESPONDENTS TO THE SURVEY, AND 21 PERCENT REPLIED THAT THE TREND IN THE VOLUME OF THEIR OUTPUT WAS UP OVER THE LAST FOUR MONTHS, 60 PERCENT REPLIED UNCHANGED AND 19 PERCENT REPLIED DOWN. THE PREVIOUS SURVEY RECORDED 27 PERCENT, 54 PERCENT AND 19 PERCENT, RESPECTIVELY. THE ONLY SECTOR IN WHICH RISING RETAIL SALES VOLUME AFFECTED SURVEY RESPONSES WAS THE PRODUCTION OF ELECTRICAL CONSUMER GOODS. THERE WAS LITTLE CHANGE IN THE RESPONSE TO CONFIDENCE QUERIES SINCE LAST APRIL'S SURVEY: 68 PERCENT OF THOSE POLLED SHOWING NO CHANGE IN THEIR CONFIDENCE (A 5 PERCENTAGE POINT RISE FROM THE PREVIOUS PERIOD) WITH A ROUGHLY EQUAL FALL IN THOSE WHO ARE LESS CONFIDENT THIS QUARTER AS COMPARED TO THE FIRST QUARTER. THERE IS CONSIDERABLE UNCERTAINTY ABOUT THE TRENDS OF FUTURE ORDERS AT HOME AND OVERSEAS THIS IS COMPOUNDED BY CONCERN ABOUT HOW THE NEW STAGE OF PAY POLICY WILL DEVELOP. THE EXPORT SECTOR, HOWEVER, DID SEEM TO BE SHOWING A SLIGHT IMPROVEMENT, WITH THE SURVEY SHOWING A MARGINAL IMPROVEMENT IN OPTIMISM ABOUT UK COMPETITIVENESS. SIMILARLY, THE SURVEY SHOWED AN IMPROVEMENT IN THE EMPLOYMENT OUTLOOK. THE CBI SURVEY CON-

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TAINED SOME EVIDENCE THAT SMALL BUSINESSES MAY BE BEGINNING TO RESPOND TO GOVERNMENT INITIATIVES BY TAKING ON MORE LABOR AT A TIME WHEN LARGER COMPANIES ARE STILL PLANNING CUTBACKS.

SURVEY RESPONDENTS CONTINUE TO REPORT THAT THE PRIMARY CONSTRAINT TO RISING OUTPUT REMAINS THE LEVEL OF DEMAND

. OTHER THAN CONTINUED INDICATIONS OF SKILLED LABOR SHORTAGES, SUPPLY SIDE FACTORS SUCH AS RAW MATERIALS AVAILABILITY, ACCESS TO FINANCE, OR GENERAL LABOR AVAILABILITY DO NOT APPEAR TO BE HAMPERING OUTPUT.

THE CBI'S MONTHLY ECONOMIC SITUATION REPORT WHICH ACCOMPANIED THE SURVEY STATED: "WHILE WE CONTINUE TO EXPECT 1978 TO BE A YEAR OF REASONABLE GROWTH FOR THE UK ECONOMY AS A WHOLE, IT IS BECOMING INCREASINGLY LIKELY

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P R 021806Z AUG 78  
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TREASURY DEPT WASHDC PRIORITY  
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THAT THIS WILL NOT HAVE BEEN REFLECTED RIGHT THROUGH  
MANUFACTURING INDUSTRY." THIS LEADS THE CBI TO FORECAST  
THAT ON PRESENT POLICIES OUTPUT GROWTH THROUGH 1979 WILL  
DECELERATE FROM THE EXPECTED 3 TO 3.5 PERCENT TO AROUND  
2 TO 2.5 PERCENT. THIS WOULD BE ACCOMPANIED BY A SMALL  
SURPLUS IN CURRENT ACCOUNT AND BY SINGLE-FIGURE PRICE  
INFLATION FOR MOST OF NEXT YEAR.

## 2. FINANCIAL MARKETS.

THE BANK OF ENGLAND ANNOUNCED JULY 27 THAT THE RATE  
OF CALL FOR SPECIAL DEPOSITS WOULD BE REDUCED FROM 2 PER-  
CENT TO 1 PERCENT EFFECTIVE JULY 31. THIS MEASURE FOL-  
LWS A PREVIOUS TEMPORARY REDUCTION FROM 3 PERCENT. THE  
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SCHEDULED RETURN TO 3 PERCENT NOW PUTS A 1 PERCENT RECALL  
ON SEPTEMBER 11, AND A FINAL 1 PERCENT RECALL ON SEPTEMBER  
26. THIS IS ESTIMATED TO PROVIDE APPROXIMATELY  
440 MILLION POUNDS IN ADDITIONAL BANK RESERVES FOR

THE PERIOD TO SEPTEMBER 26.

THE MONEY MARKET SHORTAGES CONTINUED THROUGH THE FIRST DAYS OF THIS REPORTING WEEK, AND THE YIELD CURVE ON SHORT-TERM RATES SHOWED A CLEAR NEGATIVE SLOPE. A MAJOR CONTRIBUTION TO THE SHORTAGE WAS A HIGH LEVEL OF TAX PAYMENTS, AND THE BANK OF ENGLAND PROVIDED SUBSTANTIAL ASSISTANCE TO THE MARKET, PARTICULARLY ON MONDAY. THE REDUCTION OF THE RATE OF CALL ON SPECIAL DEPOSITS AND THE BANK OF ENGLAND ASSISTANCE, WHICH SOME MARKET SOURCES CHARACTERIZED AS SOMEWHAT OVERDONE, APPEARED TO EASE PRESSURES ON THE MARKET CONSIDERABLY. MONEY MARKET RATES DRIFTED DOWN IN CONSEQUENCE OVER A HALF PERCENT, AND THE YIELD CURVE APPEARED TO FLATTEN.

GILT PRICES SHOWED LITTLE DIRECTION OVER THE WEEK. THE REDUCTION IN THE CALL FOR SPECIAL DEPOSITS PUT UPWARD PRESSURE ON PRICES, BUT THE ANNOUNCEMENT OF A LONG NEW ISSUE COUNTERED THIS. 800 MILLION POUNDS OF THE NEW ISSUE, THE EXCHEQUER 12 PERCENT 1999-2002, WAS OFFERED TODAY, PRICED AT 96 POUNDS (PER ONE HUNDRED POUNDS NOMINAL VALUE). OF THE 96 POUNDS, 15 POUNDS WAS PAYABLE ON APPLICATION, 40 POUNDS AUGUST 22, AND 41 POUNDS SEPTEMBER 18. MARKET SOURCES ESTIMATE THAT VERY LITTLE, PERHAPS 100 MILLION POUNDS, OF THE NEW GILT WAS SOLD TODAY.

3. STERLING TENDED TO SIT ON THE SIDELINES AS ACTIVITY CENTERED ON THE DOLLAR/YEN AND SWISSY RATES, AND THE SHARP INCREASE IN THE GOLD PRICE, WITH HEAVY DEMAND BEING CITED. THE FOREIGN EXCHANGE MARKETS BELIEVE THAT THE FED AND BUNDESBANK HAVE BEEN INTERVENING FAIRLY SUBSTANTIALLY.  
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DEALERS SAY THE RELEASE OF SPECIAL DEPOSITS HAS TENDED TO TAKE THE STEAM OUT OF STERLING, HELPING TO EASE PRESSURE ON INTEREST RATES, AND IN TURN HELPING TO BRING BETTER BALANCE TO STERLING IN THE FOREIGN EXCHANGE MARKETS. VOLUME FOR STERLING HAS BEEN VERY LOW, WITH EUROPEAN MARKETS GENERALLY TERMED DIFFICULT TO ASSESS BECAUSE OF VACATIONS, FACTORY CLOSURES, ABSENCES OF KEY PLAYERS AND MANAGEMENT, ETC.

THE RISE IN RESERVES ON JULY OF \$193 MILLION (TO \$16.73 BILLION) WITH AN UNDERLYING INCREASE OF \$328 MILLION WAS CONSIDERABLY BELOW MARKET EXPECTATIONS, CAUSING SOME DEALERS TO WONDER ABOUT THE DEGREE TO WHICH THE BANK OF ENGLAND OR THE MARKET HAS TENDED TO "CAP" STERLING IN THE \$1.94 RANGE. DEALERS ANTICIPATE THE BANK OF ENGLAND WILL ATTEMPT TO MAINTAIN A FAIRLY STABLE RATE BETWEEN NOW AND THE EXPECTED OCTOBER ELECTION.

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P R 021806Z AUG 78  
FM AMEMBASSY LONDON  
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#### 4. EXCHANGE RATE AND GOLD EFFECTIVE

| EXCHANGE RATE                               |                    |                           |           |
|---------------------------------------------|--------------------|---------------------------|-----------|
| DATE                                        | EXCHANGE RATE (\$) | (DEC. 1971<br>EQUALS 100) | GOLD (\$) |
| 7/26                                        | 1.9120             | 62.3                      | 194-3/8   |
| 7/27                                        | 1.9075             | 62.2                      | 194-1/8   |
| 7/28                                        | 1.9250             | 62.5                      | 201-5/8   |
| 7/31                                        | 1.9315             | 62.5                      | 200-5/8   |
| 8/1                                         | 1.9270             | 62.3                      | 202-7/8   |
| CHANGE 7/25-8/1 UP 0.0005 DOWN 0.5 UP 8-1/2 |                    |                           |           |

#### 5. FORWARD PREMIUM ON STERLING

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| DATE            | 1 MONTH | 3 MONTHS | 6 MONTHS |
|-----------------|---------|----------|----------|
| 7/26            | - 0.52  | - 1.25   | - 2.30   |
| 7/27            | - 0.48  | - 1.22   | - 2.28   |
| 7/28            | - 0.37  | - 1.17   | - 2.15   |
| 7/31            | - 0.45  | - 1.12   | - 2.05   |
| 8/1             | - 0.42  | - 1.02   | - 2.05   |
| CHANGE 7/25-8/1 | UP 0.03 | UP 0.06  | UP 0.06  |

(ALL FIGURES IN CENTS)

## 6. EURODOLLAR INTEREST RATES

| DATE            | 1 MONTH  | 3 MONTHS | 6 MONTHS  |
|-----------------|----------|----------|-----------|
| 7/26            | 7-5/8    | 8-3/8    | 9         |
| 7/27            | 8-1/8    | 8-1/2    | 9-1/16    |
| 7/28            | 8-13/16  | 8-1/2    | 9         |
| 7/31            | 8-1/8    | 8-3/8    | 9         |
| 8/1             | 8        | 8-1/2    | 9         |
| CHANGE 7/25-8/1 | DOWN 1/8 | DOWN 1/4 | DOWN 1/16 |

## 7. THREE-MONTH LONDON INTERBANK - EURODOLLAR INTEREST RATE DIFFERENTIAL

| DATE            |           |
|-----------------|-----------|
| 7/26            | 1-13/16   |
| 7/27            | 1-21/32   |
| 7/28            | 1-19/32   |
| 7/31            | 1-3/8     |
| 8/1             | 1-5/16    |
| CHANGE 7/25-8/1 | DOWN 5/16 |

## 8. STERLING CERTIFICATES OF DEPOSIT

| DATE | 1 MONTH | 3 MONTHS | 6 MONTHS |
|------|---------|----------|----------|
| 7/26 | 10-5/16 | 10-1/16  | 10       |
| 7/27 | 10-3/32 | 9-29/32  | 9-15/16  |
| 7/28 | 9-29/32 | 9-7/8    | 9-15/16  |

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|                 |          |            |          |
|-----------------|----------|------------|----------|
| 7/31            | 9-25/32  | 9-41/64    | 9-23/32  |
| 8/1             | 9-13/16  | 9-19/32    | 9-11/16  |
| CHANGE 7/25-8/1 | DOWN 5/8 | DOWN 19/32 | DOWN 1/2 |

## 9. INTERPOLATED REDEMPTION YIELDS OF HIGH COUPON GOVERNMENT SECURITIES

| DATE            | 5 YEARS   | 15 YEARS | 25 YEARS |
|-----------------|-----------|----------|----------|
| 7/26            | 11.51     | 12.55    | 12.78    |
| 7/27            | 11.50     | 12.57    | 12.81    |
| 7/28            | 11.47     | 12.59    | 12.82    |
| 7/31            | 11.46     | 12.58    | 12.84    |
| 8/1             | 11.43     | 12.55    | 12.81    |
| CHANGE 7/25-8/1 | DOWN 0.02 | UP 0.04  | UP 0.06  |

## 10. THE MINIMUM LENDING RATE REMAINS 10 PERCENT AS SET

JUNE 8 BY THE BANK OF ENGLAND.

11. THE TREASURY BILL RATE FELL 0.1294 PERCENT TO 9.1136 PERCENT AT FRIDAY'S TREASURY BILL AUCTION, A TOTAL OF 684.17 MILLION POUNDS IN BIDS BEING RECEIVED FOR THE 300 MILLION POUNDS IN BILLS OFFERED. THIS WEEK 400 MILLION POUNDS IN BILLS WILL BE OFFERED AS 500 MILLION POUNDS MATURE.

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## Message Attributes

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**Review Content Flags:**  
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**Type:** TE  
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